Tax Treatment of Dividend from FY 2020-21

A **dividend** is a distribution of profits by a company to its shareholders. When a company earns a profit or surplus, it is able to pay a proportion of the profit as a dividend to its shareholders. However, as per Income Tax Act, 1961 dividend also includes bonus shares and debentures to preference shareholders, distribution on liquidation to the extent attributable to the accumulated profits of the company immediately before its liquidation and also includes any advance or loan by a closely held company to its shareholder who is the beneficial owner of 10% or more equity capital in the company.

Up to FY 2019-20, if a shareholder gets dividend from a domestic company then he shall not be liable to pay any tax on such dividend as it is exempt from tax under section 10(34) of the Act. However, in such cases, the domestic company was liable to pay a Dividend Distribution Tax (DDT) under section 115-O. The Finance Act, 2020 has abolished the DDT and has moved to the classical system of taxation, wherein **dividends are taxed in the hands of investors**. So, **dividend** received from **mutual funds** held is also **taxable** in the hands of investors.

The **final dividend** including deemed dividend shall be taxable in the year in which it is declared, distributed or paid by the company, whichever is earlier. Whereas, **interim dividend** is chargeable to tax on receipt basis.

I. Taxability in the hands of a resident shareholder:

A person can deal in securities either as a trader or as an investor. To understand the implications better, let's focus on them individually:

(a)Trader:

- The income earned by him from the trading activities is taxable under the head business income. Thus, dividend from those shares, held for trading purposes is also taxed under **PGBP**.
- The assessee can claim the **deductions** of **all those expenditures** which have been incurred to earn that dividend income such as collection charges, interest on loan etc.

(b) Investor:

- Whereas, if shares are held as an investment then income arising in the nature of dividend shall be taxable under the head **other sources**.
- The assessee can claim deduction of only **interest expenditure** which has been incurred to earn that dividend income to the extent of **20% of total dividend income**. No deduction shall be allowed for any other expenses, including commission or remuneration paid to a banker or any other person for the purpose of realising such dividend.

The dividend income shall be chargeable to tax at normal tax rates as applicable in case of resident individuals.

Exception:

Where a resident individual, being an **employee of** an Indian company or its subsidiary engaged in Information technology, entertainment, pharmaceutical or bio-technology industry, receives dividend in respect of **GDRs** issued by such company under an **Employees' Stock Option Scheme**, dividend shall be taxable at concessional tax rate of **10%** without providing for any deduction under the Income-tax Act. However, the GDRs should be purchased by the employee in **foreign currency**.

II. Taxability in the hands of a non-resident shareholder:

The relevant sections under which tax is charged are as under

Section	Assessee	Particulars	Tax Rate
S. 115 AC	Non-Resident	Dividend on GDRs of an Indian Company or Public Sector Company (PSU) purchased in foreign currency	10%
S. 115 AD	Foreign Portfolio Investors	Dividend income from securities (other than income from units of specified mutual fund or units of UTI purchased in foreign currency)	20%
S. 115 E	Non-Resident Indian	Dividend income from shares of an Indian company purchased in foreign currency.	20%
S. 115 A	Non-Resident or Foreign co.	Dividend income in any other case	20%

III. Withholding of Tax:

Though the domestic companies shall not be liable to pay DDT on dividend distributed to shareholders on or after 01-04-2020, they shall be liable to deduct tax before paying dividend to its shareholders.

(a) For Resident Shareholders:

As per the Section 194, which shall be applicable to dividend distributed, declared or paid on or after 01-04-2020, an Indian company shall deduct tax at the rate of **10%** from dividend distributed to the resident shareholders if the aggregate amount of dividend distributed or paid during the financial year to a shareholder exceeds **Rs. 5,000**. (Concessional *rate of 7.50 % for the period 14th May 2020 to 31st March 2021 as per Press Release of CBDT dated 13th May, 2020)*

The **same rates** of TDS are also applicable for **mutual funds**, as per section **194K**. However, no tax shall be required to be deducted from the dividend payable to Life Insurance Corporation of India (**LIC**), General Insurance Corporation of India (**GIC**) or **any other insurer** in respect of any shares owned by it or in which it has **full beneficial interest.**

Declaration under **Form 15G/ 15H** can be filed by the individual, for nil deduction of TDS, if the total dividend income does not exceed the maximum exemption limit and tax on the estimated total income for the financial year in which such income is to be included is nil.

(b) For Non-Resident Shareholders:

Section (chargeability of income)	Section (withholding of tax)	Nature of Income	Rate of TDS (Payee is any other non-resident)	Rate of TDS (Payee is a foreign company)
S. 115 AC	Section 196C	Dividend on GDRs of an Indian Company or Public Sector Company (PSU) purchased in foreign currency	10%	10%
S. 115 AD	Section 196D	Dividend income of FPIs from securities	20%	20%
S. 115 E	Section 195	Dividend income of non-resident Indian from shares of an Indian company purchased in foreign currency.	20%	-
S. 115 A	Section 195	Dividend income of a non-resident in any other case	30%	40%

Note:
If the withholding tax rate as per DTAA is lower than the rate prescribed under the Finance Act then tax shall be deducted at the rate prescribed under ***DTAA****.*

IV. Inter-Corporate Dividend:

(a) Domestic co. receives dividend from another domestic co.:
The provisions of newly introduced section 80M removes the cascading effect by providing that inter corporate dividend shall be reduced from total income of company receiving the dividend, if same is further distributed to shareholders one month prior to the due date of filing of return.

(b) **Domestic co. receives dividend from a foreign co.:**

Dividend received by a domestic company from a foreign company, in which such domestic company has **26% or more equity shareholding**, is taxable at a rate of **15% plus Surcharge and Health and Education Cess under Section 115BBD**. Such tax shall be computed on a gross basis **without allowing deduction** for any expenditure.

Dividend received by a domestic company from a foreign company, in which equity shareholding of such domestic company is **less than 26%,** is taxable at **normal tax rate**. The domestic company **can claim deduction** for any expense incurred by it for the purposes of earning such dividend income.